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cutting through complexity

TAX

Provisional tax for individuals

Managing your tax instalment payments

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Tax impact of being a provisional taxpayer

A provisional taxpayer is required to pay instalments of income tax (called provisional tax) during the income year, rather than at the end of the year when a tax return is filed. This obligation to pay provisional tax can arise in addition to the taxpayer's employer deducting tax from salary payments.

If you are a provisional taxpayer, it is important that you make adequate provisional tax instalments during the year in order to minimise penalties and interest that may be imposed. However it can be difficult to know how much provisional tax to pay.

What type of income may cause provisional tax payments?

Income that does not have sufficient tax deducted at the time of payment can create a provisional tax liability.

Examples include:

» Employee share benefit plans

» Net rental income

» Financial arrangement income (e.g. foreign exchange gains made on foreign denominated 'debt'. Debt includes term deposits, bonds and mortgages)

» Foreign investment fund income (i.e. income from foreign shares or unit trusts, foreign life insurance)

» Foreign dividends with insufficient witholding taxes attached (note that Australian franking credits are not creditable in New Zealand)

» WIthdrawal from foreign superannuation scheme

What is provisional tax?

Provisional taxes are tax payments made throughout an income year. They go towards the tax payable on income with no tax credits attached.

Provisional tax payments can be made up of:

» Amounts that you must pay under the provisional tax rules

» Amounts you choose to pay as voluntary payments to mitigate interest any exposure you might have.

Who is obliged to pay provisional tax?

You will be a provisional taxpayer if your residual income tax liability (RIT) is greater than $2,500 in the previous income year.

Broadly speaking, your RIT is your income tax liability remaining after deducting any tax credits you have - such as PAYE, imputation credits, withholding tax credits and foreign tax credits.

Who should make voluntary payments of provisional tax?

Even if you are not normally a provisional tax payer, you might want to make voluntary provisional tax payments to prevent 'use of money interest' being imposed. This may apply if your RIT for the current year will be $50,000 or more.

If you are a provisional taxpayer, you might also choose to make voluntary payments if you expect your income to be higher than in the previous year.

When is provisional tax due?

Provisional tax is generally due in three instalments. For individual taxpayers with a standard balance date of 31 March, the due dates for the 2016 income year are:

28 AUG 2015

15 JAN 2016

07 MAY 2016

How is provisional tax calculated?

The provisional tax rules set out how to calculate the amount of provisional tax you are obliged to pay. This can be done using an 'uplift method', or by making a formal estimate of your RIT for the year.

There is also an option to calculate and pay provisional tax based on your GST position, if you are registered for GST. This document does not address the provisional tax rules applying to GST registered taxpayers - please ask your KPMG advisor.

Residual Income Tax (RIT)

RIT is the tax due after allowing for tax credits but before allowing for any provisional tax payments made.

FOR EXAMPLE:

Salary	200,000	
Interest	10,000	
Net rental income	20,000	
Total taxable income		230,000
Tax on taxable income		66,820
Less: Tax credits		
PAYE	56,920	
RWT	3,300	60,220
Residual income tax		**6,600**
Provisional tax		5,000
Terminal tax		**1,600**

The amounts for 2016 provisional tax instalments are:

Scenarios	Instalment 1 (P1)	Instalment 2 (P2)	Instalment 3 (P3)
If 2015 not filed	(2014 RIT x 110% x 1/3)	(2014 RIT x 110% x 2/3) Less amount paid at P1	(2015 RIT x 105%) Less amount paid at P1 and P2
If 2015 is filed	(2015 RIT x 105% x 1/3)	(2015 RIT x 105% x 2/3) Less amount paid at P1	(2015 RIT x 105%) Less amount paid at P1 and P2
If estimate made	Estimate x 1/3	Estimate x 2/3 Less amount paid at P1	Estimate less amount paid at P1 and P2

Penalties and interest

Penalties and/or interest may be charged on underpayments of provisional tax.

Penalties are based on the lower of:

» Provisional tax calculated under the standard uplift calculation (or your estimate if you have filed one) at each instalment; or

» Actual RIT spread across the three instalment dates.

Penalties are broadly 5 percent of the unpaid tax, followed by 1 percent increments each month thereafter until the date of payment. Unpaid tax includes any penalties charged.

Use of money interest can also be charged where the individual has a RIT of $50,000 or more, or has filed an estimate with Inland Revenue for provisional tax.

Interest applies to the under-payment at each instalment and is calculated comparing one third of the actual RIT with the amount paid at each instalment.

Exemptions

You are not obliged to pay provisional tax if your RIT for the preceding income year is less than $2,500. However, payments may still be required to mitigate interest if your RIT is expected to be $50,000 or more.

Estimate

If you consider the payment due under the standard calculation will not reflect your actual liability, you may base your payments on an estimate.

Depending on the amount due using the standard calculation method, you might need to file an estimation form with Inland Revenue to advise them of your estimated RIT. The estimate must be fair and reasonable, otherwise penalties may be imposed.

The estimate filed is the amount you expect your RIT to be for the full year. The amounts due at each instalment are:

P1 – Instalment 1
Estimate x ⅓

P2 – Instalment 2
(Estimate x ⅔) – (P1 payment)

P3 – Instalment 3
(Estimate) – (P1 + P2 payments)

Using an estimate will expose you to use of money interest, even if your RIT is less then $50,000. Therefore, you should obtain advice before electing to make a formal estimate.

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